

# Solving the affordable housing crisis: Turning InvestEU into a success story

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In recent years, the affordable housing market has been squeezed between a rock and a hard place. Housing needs have increased in most of the EU's urban areas. Meanwhile, there has been a decline in investment, in terms of the absence of new construction projects and renovation projects.

Using the insights gathered through the activities of the EPC Task Force on Affordable and decent housing solutions, this Policy Brief lays down a set of recommendations to strengthen the delivery of InvestEU, and guide member states and EU institutions to better funnel investment to reach those most in need.

InvestEU offers an opportunity to curb this unequal supply-and-demand relationship in affordable housing significantly. However, to become a success story, the European Investment Advisory Hub (EIAH) must invest more in capacity building, to help develop bankable projects and investment platforms. Member states must increase public support for housing and use innovative financing instruments to 'de-risk' investment. Finally, the European Commission should clarify the 'dos and don'ts' under European regulation.

## BACKGROUND: THE BROKEN RELATIONSHIP BETWEEN SUPPLY AND DEMAND

On the **demand** side, at least 700,000 people experience **homelessness** on any given night in the EU; a 70% growth rate compared to the last decade.<sup>1</sup> **Housing cost overburden** – where households spend over 40% of their disposable income on housing – has increased for some social groups. In 2019, 35.4% of EU27 low- to medium-income families were burdened, compared to 9.4% of total households. Between 2010 and 2019, while overburden grew for lower-income families (+1.7%), the reverse was true for the rest of the population (-6.3%), showcasing the polarisation of the European housing market.<sup>2</sup>

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There have been significant improvements in the past decade on some fronts. However, they remain a point of concern for some. For example, **energy poverty** remains an issue: 18.2% of poorer households still struggle to maintain ideal room temperature in 2019.<sup>3</sup> The same applies to **the quality of housing arrangements**. Lower-income families are more likely to live in overcrowded conditions (29.1%) or lack adequate amenities like a shower or indoor toilet (9.5%) than the total European population (17.2% and 4.0% respectively).<sup>4</sup>

On the **supply** side, public investment in affordable housing has declined across the EU27. From 2008 to 2018, public expenditure on **housing development** decreased by -27.8%, from €29 to €21 billion.<sup>5</sup> The investment gap in affordable housing in the EU is estimated to be around €57 billion per year,<sup>6</sup> subsequently exacerbating the ageing and deterioration of the existing housing supply.

Due to this reduction, **private investment** has become more crucial than ever. However, several factors hinder filling this investment gap. High land prices in major European cities and the industry shift from housing as a place to build a home, to housing as an investment, make for high construction costs. This means that the sector is **capital-intensive**. Furthermore, the investment returns are low, which discourages risk-averse investors and those who prioritise short-term gains.<sup>7</sup> Revenue structures usually comprise rental income (which is always below market value) and government rent subsidies. However, high construction costs restrict the degree to which rent can be made sufficiently affordable for low- and middle-income households and the time needed to recuperate the investment.<sup>8</sup>

Furthermore, while **EU housing payments** have increased by +13% between 2008 and 2018, there are vast national differences. France and Ireland spent almost 1% of their GDP, while 10 countries spent close to 0%.<sup>9</sup> Due to this interplay, private investors participate more in intermediate and/or affordable housing schemes than in social housing with very low rent.<sup>10</sup>

## STATE OF PLAY: CLOSING THE GAP THROUGH INVESTEU

Having identified these issues, the European Commission, together with the European Investment Bank (EIB), set up the Investment Plan for Europe to curb the negative investment trend following the 2008 financial crisis. A vital pillar of the Plan was the European Fund for Strategic Investments (EFSI), an EU guarantee of €33.5 billion. An additional €500 billion was channelled through the EFSI to various sectors of the economy, including affordable housing, between 2015 and 2020.<sup>11</sup>

Building on the precedent's success, in 2018, the Commission announced InvestEU, a more ambitious investment plan. Using the same tactics and an upgraded guarantee of €75 billion, it is expected to raise €1 trillion in additional investment between 2021 and 2027. More specifically, InvestEU has identified social investment and skills as areas in need of intervention and has set aside €3.6 billion for them.

Investment will also be channelled into building additional housing infrastructure. However, this is not the only window of relevance to the affordable housing market. With a budget of €20 billion, investment in sustainable infrastructure can be directed towards renovation projects focused on energy savings and the modernisation of ageing affordable housing.<sup>12</sup>

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InvestEU provides an opportunity that the affordable housing sector must seize. However, more finetuning is required to ensure that it meets the actual investment demands of organisations on the ground and boosts their capacity to develop investable propositions.

## PROSPECTS: INVESTMENT REACHING THOSE IN NEED

How can the delivery of InvestEU be strengthened so that it overcomes the mistakes made by its predecessor? How should member states and EU institutions funnel investment to better reach those most in need?

### *Build the capacity to develop bankable projects*

Under the preceding Investment Plan, most investments were concentrated in several of the larger EU countries. By the end of 2017, around 82% of all signed EFSI financing went towards the EU15.<sup>13</sup> This was largely due to the demand-driven nature of the Plan: organisations had to propose viable projects to the EIB. In countries lacking national promotional banks and institutions (NPBIs) – which can develop projects and co-finance and attract additional investment –, financing could not always reach those needing it.

Given that InvestEU shares the same blueprint as the EFSI, the EIAH must prioritise capacity building to ensure that investment is shared among the EU27 equitably. The EIAH signing memoranda of understanding (MoUs) with various institutions across the EU member states – to share knowledge, deliver services locally or act as local points of entry – proved a potent strategy for curbing the regional inequalities of the past investment plan.<sup>14</sup> Nonetheless, to date, not all priority areas of InvestEU are covered in these MoUs. The EIAH should reach out to potential intermediaries more proactively, to have a local presence that can steer investment under all priority areas in every country.

One potential avenue is establishing capacity-building relations with government agencies and/or ministries of countries lacking NPBI. For example, while Romania does not have a national promotional bank (NPB), its Ministry of Finance can issue public guarantees for public-private partnerships and bridge the EIB and organisations wanting to invest in affordable housing solutions. However, NPBI and national governments have varying degrees of willingness or capacity to collaborate with the EIAH.<sup>15</sup> For this solution to work, member states must take on their share of responsibility by tackling the issue in their national recovery and resilience plans, and focus on institutional reforms aimed at boosting their absorption capacities of EU investment funds.

#### *Fulfil the potential of investment platforms*

Due to the instrument's design, it may prove difficult for small-scale organisations to comply with the financial conditions of the InvestEU loan. The EIB can finance up to 50% of a project, with the minimum loan amount set to €25 million. These conditions could be challenging for smaller cities or housing associations if they lack the finances to fund the remainder of the project. A solution for circumventing this problem is investment platforms: grouping several stakeholders from a sector to finance smaller projects, share risks, and combine EU and national support with private investment. Nevertheless, despite their recognition as a powerful solution, their potential remains unfulfilled.

One success story is the European Alliance for Sustainable and Inclusive Social Housing in France, where the French NPB and an organisation representing housing providers have built an investment alliance. This acts as a single contact point for social landlords in France and facilitates better access to funding from InvestEU and the Council of Europe Development Bank. This good practice should be exported throughout the EU27.

However, while not mandatory, a project leader from the public sector is often needed to set up such platforms. As such, there is a threat of investment remaining concentrated in countries with strong NPBI. Other actors, such as private stakeholders, could take on leading roles in their absence. Commercial banks are already investing in small-scale affordable housing projects with the EIB.<sup>16</sup> To increase the number of private institutions taking the role of investment platform project promoter, the EIAH should invest more in capacity building. This can be achieved by cooperating with national institutions on awareness-raising campaigns to attract commercial banks' interest and incentivise them to propose projects.

#### *De-risk investment*

Besides collaborating on strengthening capacity building, member states are also responsible for enhancing their national welfare systems so that affordable housing is a secure and predictable market for the private sector. They should pay more attention to revenue streams. In countries with robust housing

systems, homeless people and those with low income are likely to receive housing benefits for a long time. This provides a secure opportunity for investors. Without welfare payments, rent ends up financing the majority of investment. Tenancy then becomes unaffordable for a significant proportion of households.

Given the vast disparities in social housing allocation amid government budget consolidations, member states must strengthen their welfare systems to deliver affordable and decent housing solutions for those most in need. However, this should not be done as an alternative to public housing development. As mentioned, although a crucial piece of the puzzle, private investment is not a silver bullet for providing housing to the most vulnerable social groups. The current investment gap calls for more public support in both private investment and public housing. France serves as a good example again, having expanded its spending on both housing benefits and development projects.

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The EU27 should also follow and replicate the most recent financial innovations to drive capital into the affordable housing market. For example, outcomes funds are used to de-risk investment for public and private entities. The latter only repay the investment cost if specific social outcomes, usually related to improving social services' delivery efficiency and effectiveness, are achieved. Key social indicators of financing projects typically go through several evaluations, and recommendations are issued to improve results.<sup>17</sup> Investment initiatives become more sustainable and impactful thanks to these interventions. Furthermore, outcomes funds present a double advantage for national governments, as they can blend various national and European funds.

#### *Clarify the dos and don'ts under EU regulation*

To curb the unequal relationship between affordable housing supply and demand, the European Commission must clarify the dos and don'ts of state aid. Under current state aid regulations, *social housing* is defined as housing for disadvantaged citizens and/or socially less advantaged groups who cannot obtain housing at market conditions due to solvency constraints.<sup>18</sup> Many argue that regulators should enlarge this definition so that governments can invest in affordable housing infrastructure according to their national traditions and without breaching state aid rules. However, it must be stated that member states

already have the autonomy to define their target groups according to their traditions. Furthermore, removing any mention of a target group from the EU definition could have the undesired effect of member states channelling investment away from the most vulnerable people.

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Even so, some countries consider the *social housing* definition ambiguous and argue that it prevents them from investing in their affordable housing infrastructure. To deal with this de facto investment barrier, the Commission should issue another decision on the application of the definition, to clarify the degree to which national traditions can be incorporated in setting target groups.

## CONCLUSION

Solving the broken relationship between the supply of and demand for affordable housing in Europe is crucial, given the rising number of homelessness and low-income households burdened by housing costs. InvestEU provides an opportunity to increase new affordable housing and renovate the existing supply. Nevertheless, this instrument's success should not be taken for granted. Should the weaknesses of the preceding Investment Plan for Europe not be addressed, it would be at the expense of vulnerable people in dire need of housing.

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